

**Testimony of Tom Lund**  
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**Before the U.S. House Committee on Financial Services**  
**Hearing on “Impact on Homebuyers and Housing Market of Conforming Loan Limit Increase”**

**May 22, 2008**  
**Washington, D.C.**

Thank you Chairman Frank, Ranking Member Bachus, and Members of the Committee for inviting me today.

This Committee recognized the need for increasing the conforming loan limit in high-cost areas long before the housing crisis began. Under the leadership of Chairman Frank and Representative Gary Miller, this Committee included an increase in the high-cost area loan limit in the GSE regulatory reform bill the House passed last spring with bipartisan support.

A higher limit in high-cost areas reflects the realities of today’s housing market. That is, while the conforming loan limit is a national standard, wide regional disparities exist in housing affordability in this country.

The liquidity crisis in mortgages has given added impetus to expanding the conforming loan limit in high-cost areas. As the correction took hold last fall and winter, jumbo and other non-conforming lending all but ground to a halt in many markets. Meanwhile, the conforming market served by Fannie Mae and Freddie Mac continued to operate well, and in fact our credit book has expanded during the downturn. Fannie Mae continues to extend credit in every state in the union, in cities and in rural communities across the country, so that creditworthy borrowers can buy and own a home.

Congress and the President took a positive step toward providing more liquidity to the jumbo market in February with the passage of the Economic Stimulus Act. For the first time, the benefits of the conforming market were extended to middle-income families seeking to afford homes in high-cost areas. However, the extension is currently scheduled to sunset at the end of this year.

Our goal was to begin accepting loans within 30 days of HUD publishing the list of MSAs eligible for jumbo-conforming loans — which we did.

Six weeks into the initiative, we have purchased or guaranteed a relatively small number of jumbo-conforming loans. There are two reasons why. One is time. As with any new product, both Fannie Mae and its lender partners need to implement new policies and procedures to identify and deliver a new form of conforming loan. Then there is the time between loan application, loan closing and delivery in the secondary market. All in, this can take between 30 and 120 days.

The second reason has to do with how the secondary market is structured. Jumbo-conforming loans are not eligible to be delivered in the most liquid, efficient part of the secondary mortgage market. That is the so-called “TBA” market, or to-be-announced, which is a designation that conventional, conforming loans enjoy that allows lenders to make a conforming loan with absolute certainty that it can be securitized at a later date. This certainty makes the funding and delivery of these loans extremely efficient and liquid, and delivers the lowest-cost conforming loan possible for a borrower based on their credit risk.

Based in part on the temporary nature of the conforming loan limit extension, the Securities Industry and Financial Markets Association made the decision to exclude jumbo-conforming from TBA-eligible pools. We feel this exclusion is one reason why lenders were reluctant, in the weeks after the Stimulus Act was enacted, to make jumbo-conforming loans at rates closer to traditional conforming loans. Without the TBA designation, lenders were unsure of secondary market execution, and thus demanded higher fees and pricing to cover the extra costs and risks. That said, our entrance into the market did provide some relief – approximately half a point in the rate offered to borrowers compared to the non-agency jumbo market.

To go further in helping alleviate this problem, on May 6 Fannie Mae announced that we would purchase jumbo-conforming loans for our portfolio without demanding the non-TBA, on-top liquidity premium. This means that while jumbo-conforming loans are not TBA-eligible, we are pricing them as if they were, and have committed to doing so through the end of this year. While every borrower’s rate is set by a variety of risk factors, we view it as our responsibility to make sure that a lack of liquidity in the jumbo market is not one of them.

To put the May 6 announcement in context: At the height of the jumbo loan liquidity crunch, jumbo loans were commanding a yield of as much 1.25 points higher than standard conforming loans. Since our announcement, jumbo-conforming loans have improved to between flat and one-eighth above standard conforming. For an average consumer of a \$700,000 loan in a high-cost MSA, these rate reductions equate to savings of more than \$400 a month.

As a result of this change, our pipelines for future delivery of jumbo-conforming loans have grown rapidly in the last two weeks. I would also point out that it was our ability to bring these jumbo-conforming loans into our portfolio that allowed us to make this beneficial move.

Fannie Mae’s decision to absorb the liquidity premium lasts until the end of this year, when the conforming loan limit provisions of the Stimulus Act expire. In our view, the temporary nature of the law is a major hindrance to the development of an efficient, liquid market for jumbo-conforming loans.

A window of seven months is not enough time to create an asset class with the liquidity and scope that traditional conforming mortgages enjoy. A permanent high-cost area loan

limit would, we believe, be an extremely powerful market incentive for the mortgage industry and secondary market investors to make these loans more widely available and affordable for consumers — both now and in the long term. Mr. Chairman, the House recognized this need a few weeks ago when it voted to permanently increase the conforming loan limit for high-cost areas in H.R. 3221.

Fannie Mae is working with its lender partners and the nation's housing finance industry to find ways to extend our liquidity mission to more homeowners in high-cost areas and elsewhere as the market correction plays out. We are committed to working with this Committee and others to doing all we can for the market.

Thank you again for inviting me to speak, and I look forward to your questions.